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Cases, Regulations and Statutes

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[6] See n. 2 *supra*.
[7] See n. 4 *supra*.
[8] See I.R.C. § 1221.
[9] Temp. Treas. Reg. § 1.1221-2T.
[10] Temp. Treas. Reg. § 1.1221-2T.
[11] Prop. Treas. Reg. § 1.1221-2.
[12] Prop. Treas. Reg. § 1.446-4.
[13] *Id*.
[14] Prop. Treas. Reg. § 1.446-4(a)(1). See I.R.C. § 448(c).
[15] Temp. Treas. Reg. § 1.1221-2T(b)(2).

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

BANKRUPTCY

GENERAL

AUTOMATIC STAY. The debtors had defaulted on loans secured by real property and the mortgage had been foreclosed and the property sold. The period of redemption had expired and all that was left to complete the transfer of title was a judicial confirmation of the sale. Before this could occur, the debtors filed for bankruptcy. The court held that the automatic stay barred the judicial confirmation of the sale until the creditor obtained relief from the automatic stay. **U.S. v. Molitor, 157 B.R. 427 (W.D. Wis. 1992)**.

EXEMPTIONS-*ALM* § 13.03[3]*

ANNUITY. Prior to filing for bankruptcy, the debtor sold some non-exempt assets and purchased three annuity contracts. The debtor claimed the three contracts as exempt under Calif. Code of Civ. Proc. § 704.100(c). The court held that the annuity contracts were not eligible for the exemption because the annuities did not represent benefit payments from matured life insurance policies. ***In re* Pikush, 157 B.R. 155 (Bankr. 9th Cir. 1993)**.

AVOIDABLE LIENS. The debtor claimed a homestead exemption under Section 522(f) and sought to avoid judicial liens which impaired the exemption. The liens against the house included a first priority unavoidable mortgage, four next priority judicial liens and a sixth priority unavoidable tax lien. The total of the liens substantially exceeded the value of the house. The creditor argued that because the first and sixth priority liens were unavoidable and exceeded the value of the house, the judicial liens did not impair the exemption. The court held that the impairment occurred when the liens, taken in order of priority, first exceeded the value of the house less the exemption amount; however, the impairment only affected the priority of the liens by placing the debtor's exemption amount in the priority scheme. Because the IRS lien could not be affected by the change in priority, the last judicial lien was bifurcated into a seventh priority portion equal to the exemption amount. The affect of this solution is that (1) no actual avoidance of a lien occurs but the debtor receives the exemption amount upon sale of the collateral and (2) the lien which caused the total of liens to exceed the value of the exempt property less the exemption amount became unsecured by the exemption amount. ***In re* Bellenoit, 157 B.R. 185 (Bankr. D. Mass. 1992)**.

HOMESTEAD. The debtor had claimed a homestead exemption under Cal. Code of Civil Proc. § 703.140. The trustee objected to the exemption because the bankruptcy case was not an attempt to sell the residence to enforce a money judgment. The court held that because the Bankruptcy Code gives the trustee the status as hypothetical creditor, the exemption was allowed in a bankruptcy case. ***In re* Norman, 157 B.R. 460 (Bankr. C.D. Calif. 1993)**.

IRA. The debtor opened an IRA in 1987 and filed for bankruptcy in 1992, claiming the IRA as exempt. The debtor was 45 years old and was facing unemployment due to a shutdown of the company for which the debtor worked. The court found that the debtor's income just exceeded the debtor's expenses but after unemployment, the expenses would exceed income. However, because the debtor had never made withdrawals from the IRA and that demonstrated that the debtor did not need all of the account for living expenses, the court held that half of the account must be turned over to the trustee. The court also ordered the debtor and trustee to share in the cost of the federal taxes and penalties resulting from the early withdrawal from the IRS. ***In re* Metzner, 157 B.R. 332 (Bankr. N.D. Ohio 1993)**.

The debtor owned two IRA's, one for $2,000 and one for $5,500, which the debtor claimed as exempt. The debtor was 58 years old and on medical leave for stress. The debtor was planning to separate from her spouse and was under a threat of losing her job. The debtor had more debt payments and personal expenses than would be covered by payments from the IRAs. The court held that only the $2,000 IRA was not reasonably necessary for the debtor's support and not exempt. The debtor was required to pay any taxes and penalties resulting from the early withdrawal of funds from the IRA. ***In re* Bogart, 157 B.R. 345 (Bankr. N.D. Ohio 1993)**.

OBJECTIONS. The debtor claimed real property as exempt in the bankruptcy petition in April 1992 but did not provide any statutory basis for the exemption. In September 1992, the debtor amended the exemption schedules to include an automobile but did not otherwise amend the exemptions. The trustee filed an objection to the real property exemption in September 1992, arguing that the objection should be allowed because it was made within 30 days after an amendment to the exemptions. The court held that the objection was untimely because the amendment did not change the exemption claim for the real property. The court also held that the lack of identification of the statutory basis for the exemption did not affect the validity of the exemption once the time limit for objections had expired. ***In re* Hickman, 157 B.R. 336 (Bankr. N.D. Ohio 1993)**.

STOCK. Holdings such as in *In re Hickman, supra* have apparently led to the practice of "exemption by declaration" wherein debtors claim nonexempt property as exempt in the hope that the trustee or creditors will fail to timely object, thus creating an exemption where none was otherwise allowed. In the present case, the debtor claimed $1,192 worth of stock as exempt under the Indiana exemption for tangible personal property. The court held that the stock was clearly intangible property and the claim of the exemption was an attempt to create an exemption by declaration. In an attempt to discourage future false exemption claims, the court disallowed all of the stock as exempt, including the portion which would have been exempt under the intangible personal property exemption, and charged the bankruptcy estate's legal fees to the debtor. **Matter of Slentz, 157 B.R. 418 (Bankr. N.D. Ind. 1993)**.

CHAPTER 12-*ALM* § 13.03[8]*

DISMISSAL. The debtors filed a Chapter 12 petition and later filed to dismiss the petition. A creditor objected to the dismissal and reinstatement of the petition was ordered. The debtors appealed that decision. During the pendency of that appeal, the case was converted to Chapter 7 and all assets distributed to creditors without objection by the debtors. The court held that the appeal of the reinstatement decision was dismissed as moot. ***In re* Roller, 999 F.2d 346 (8th Cir. 1993)**.

ELIGIBILITY. The debtor owned farm land and had operated the farm for several years until the debtor's spouse formed a corporation to operate the farm. The debtor rented the land to the corporation and was employed by the corporation to drive trucks. The corporation provided the working capital for the farm operation, employed the debtor to operate the farm and paid cash rent to the debtor for use of the farm land. The corporation also paid cash rent to the debtor for the farm office and use of the debtor's machinery shop. Creditors objected to the debtor's eligibility for Chapter 12 because less than 50 percent of the debtor's income came from farming. The court rejected the test of *In re Armstrong, 812 F.2d 1024 (7th Cir. 1987), cert. denied, 484 U.S. 925 (1987)* requiring farm income to come from activities in which the debtor was at risk, thus eliminating wages from farm income for purposes of eligibility for Chapter 12. Instead, the court followed the dissent in *Armstrong* and used an all facts and circumstances test as to whether the debtor's wages from farming should be considered farm income. In the present case, the court held that the wages and rent payments were farm income because the debtor's involvement in the farm only changed its form by the use of the corporation and that in substance, the debtor still operated the farm. ***In re* Creviston, 157 B.R. 380 (Bankr. S.D. Ohio 1993)**.

CHAPTER 13

PLAN-*ALM* § 13.03[5].* The debtor's Chapter 13 plan provided for payments on loans secured by two pickups. The plan reduced the loan principal to the value of the vehicles and reduced the interest rate to 10 percent. The lower courts held that the prime rate was the guide for determining the adequacy of the interest rate on deferred payments on secured claims. The appellate court reversed, holding that the interest rate should be determined by the interest rate charged by the creditor for similar loans. The court rejected the prime rate as an adequate interest rate because the "cost of funds" approach to the interest rate did not account for additional costs to the creditor from administering the plan payments. The court treated the deferred payments as a coerced loan which entitled the creditor to receive the amount of interest it normally charges for similar loans. In remanding the case, the court noted that the contract interest rate was a good indication of the normal interest rate charged by the creditor. Thus, it appears that the court sanctions using the "contract rate" as the standard for interest rates on deferred Chapter 13 plan payments unless the debtor can demonstrate that the creditor is currently charging less for "coerced" loans. **General Motors Acceptance Corp. v. Jones, 999 F.2d 63 (3d Cir. 1993)**.

FEDERAL TAXATION-*ALM* § 13.03[7]*

AUTOMATIC STAY. The debtors had listed their federal income tax liability as a claim in their bankruptcy case and the IRS received notice of the case. The confirmed plan provided for payment of the tax claim outside of the plan. Eight months after the confirmation, the IRS sent the debtors a notice of intent to levy for the taxes in the claim. The debtors claimed that the levy notice violated the automatic stay and filed for an injunction and costs, including attorney's fees. The IRS did not claim sovereign immunity but claimed that damages were awardable only under I.R.C. § 7430. The court held that the debtors were entitled to an injunction and costs under Section 362(h) because the IRS had filed a claim in the case. ***In re* Boldman, 157 B.R. 412 (C.D. Ill. 1993), *aff'g*, 147 B.R. 448 (Bankr. C.D. Ill. 1992)**.

CLAIMS. The debtor's schedules listed the IRS as holding a priority tax claim but did not include the IRS in the list of creditors; therefore, the IRS did not receive notice of the bankruptcy filing. The debtor also did not file a claim for the tax claim until over 21 months after the bar date for claims. The court noted that if the IRS claim was allowed, that claim would take all of the bankruptcy estate and leave nothing for the unsecured creditors. In addition, the tax claim was nondischargeable. The court held that the untimely claim would not be allowed. ***In re* Mosely, 157 B.R. 490 (Bankr. N.D. Okla. 1993)**.

DISCHARGE. The debtor was a shareholder in an S corporation. The tax matters partner had signed an agreement to waive until November 1990 the limitation period on federal tax assessments for the corporation's 1983 tax year. The debtor filed the bankruptcy petition in

September 1990 and argued that the debtor's share of any additional tax assessed against the S corporation was dischargeable. The court held that the additional assessment was nondischargeable because at the time of the filing of the petition, the waiver agreement was still in effect and the IRS had time to make the assessment but for the filing of the bankruptcy case which stayed the assessment as to the debtor. ***In re* Anderson, 157 B.R. 104 (Bankr. N.D. Ohio 1993)**.

NONDEBTOR RIGHTS. The debtor and nondebtor spouse had filed joint federal income tax returns for 1988, 1989, and 1990 and the debtor included the tax claims for those years in the debtor's plan. The IRS levied against the nondebtor's wages and the debtor sought to enjoin the IRS collection efforts against the nondebtor spouse under Section 1301. The court held that Section 1301 applied only to collection of consumer debts and not taxes. **Matter of Greene, 157 B.R. 496 (Bankr. S.D. Ga. 1993)**.

POST-CONFIRMATION INTEREST. The IRS had filed a claim which included pre-petition tax and interest. The claim was disputed and appealed until the U.S. Supreme court denied certiorari of a ruling allowing the claim. The debtor's plan provided payment of all allowed claims on the later of the plan effective date or the date the claims became allowed. The IRS argued that because the claim could not be paid under the plan until the final appeal was exhausted, the payment of the claim was a deferred payment and the IRS was entitled to post-confirmation interest under Section 1129(a)(9)(C). The court held that the delay caused by the appeals did not make the payment deferred where the plan provided for immediate payment when the claim became allowed. ***In re* White Farm Equipment, Co., 157 B.R. 117 (N.D. Ill. 1993), *aff'g*, 146 B.R. 736 (Bankr. N.D. Ill. 1992)**.

PRIORITY. The debtor had filed two Chapter 11 cases with the plan confirmed in the first case. The IRS had filed claims in the first case and before the second case made several post-confirmation assessments of the same claims and for additional taxes. Two state taxing agencies made assessments during the first bankruptcy case and several assessments before the second case. The parties sought a determination of the priority of the various assessments. The court held that the IRS assessments relating to the claims included in the first bankruptcy case were ineffective to change their discharge status determined under the plan. The state assessments made during the first bankruptcy case were void for violation of the automatic stay. The remaining assessments had priority based on the date of the assessment and not the date the liens for the assessments were filed. ***In re* W.F. Monroe Cigar Co., 157 B.R. 125 (Bankr. N.D. Ill. 1993)**.

FEDERAL AGRICULTURAL PROGRAMS

DISASTER PROGRAM. The CCC has adopted as final amendments to the Disaster Payment Program and Tree Assistance Program regulations to add provisions for the 1993 programs. **58 Fed. Reg. 51757 (Oct. 5, 1993)**.

MEAT AND POULTRY PRODUCTS. The FSIS has adopted as final regulations requiring safe handling instructions on all raw meat and poultry product labels. The handling instructions are to include a rationale statement and instructions for safe storage of raw products, prevention of cross-contamination, cooking, and handling of leftovers. **58 Fed. Reg. 52856 (Oct. 12, 1993)**.

PACKERS AND STOCKYARDS ACT-*ALM* § 9.05.* The respondent was president of an unregistered livestock market agency. Although the respondent was not aware of the scheme, one of the respondent's customers used a check kiting scheme involving the respondent's agency to purchase cattle. When the plan fell through, the respondent's agency was left insolvent. The ALJ ruled that although the respondent did not perpetrate the check kiting scheme, the respondent's consent to the purchases was a willful violation of 7 U.S.C. § 213(a). The respondent was suspended from operating for one year. ***In re* Cedar Vale Sale Barn, Inc., 52 Agric. Dec. 546 (1993)**.

The respondents were officers and owners of a posted stockyard. Audits of the respondents' custodial accounts found several occasions when the custodial accounts were short due to the failure by the respondents to timely deposit consignors' proceeds from the consignment sale of livestock and for purchases made by the respondents' stockyard. Although no checks to consignors were dishonored for insufficient funds, the shortages were held to be violations of 7 U.S.C. §§ 208, 213(a). The respondents' registration was suspended for the greater of 21 days or until the custodial account shortages were removed. ***In re* Fowler Livestock Auction, Inc., 52 Agric. Dec. 558 (1993)**.

FEDERAL ESTATE AND GIFT TAX

CLAIMS AGAINST ESTATE-*ALM* § 5.04.* The decedent made several gifts of money to the decedent's children who transferred the money back to the decedent in exchange for a non-interest bearing note payable in 25 years or upon the death of the decedent. The decedent reported the gifts on federal gift tax returns. The court held that the estate could not deduct the notes as claims against the estate because the notes did not represent bona fide debts contracted for full and adequate consideration. **Est. of Flandreau v. Comm'r, 93-2 U.S. Tax Cas. (CCH) ¶ 60,137 (2d Cir. 1993), *aff'g*, T.C. Memo. 1992-173**.

DISCLAIMER. The decedent died intestate and was survived by a spouse and children. Under intestate succession, the surviving spouse was entitled to $20,000 and one-half of the remaining estate, with the other half passing to the children. The surviving spouse filed a written disclaimer of a pecuniary amount of the spouse's share of the estate equal to the amount which would fully use the decedent's unified credit. The IRS ruled that the disclaimer would be effective. **Ltr. Rul. 9338010, June 21, 1993**.

GIFTS-*ALM* § 6.01.* The taxpayer was a shareholder in a family-owned dairy corporation. On December 31, 1983, the taxpayer wrote a check to each of four children. The checks were endorsed for deposit on January 10, 1984. The taxpayer argued that the checks should be considered 1983 gifts because of the relation-back doctrine for checks delivered to donees. The IRS argued that the relation-back doctrine applied only to charitable gifts. The court noted that the relation-back doctrine was available to noncharitable gifts under *Est. of Metzger v. Comm'r, 100 T.C. 204 (1993)*, but held that *Metzger* would not be applied because no evidence was presented that the taxpayer had sufficient funds in the checking account to cover the checks on December 31, 1983. **W.H. Braun Family Partnership v. Comm'r, T.C. Memo. 1993-434**.

GROSS ESTATE-*ALM* § 5.02.* The decedent was a life beneficiary of a trust established by a predeceased spouse. The trust provided that trust income and corpus could only be distributed to the decedent and only for the decedent's care, support, maintenance and comfort. The decedent had agreed to allow the trustees to make annual gifts to other family members in amounts just under the annual exclusion amount. The IRS ruled that the gifts were included in the decedent's gross estate because the trustees had no power to make the distributions, even with the decedent's consent. The IRS ruled that the making of gifts for family estate planning purposes was not an enumerated purpose for distributions from the trust. **Ltr. Rul. 9337001, May 17, 1993**.

MARITAL DEDUCTION-*ALM* § 5.04[3].* The decedent's will provided for property passing to the surviving spouse in trust. The trust was funded with as much property as necessary to reduce the decedent's federal estate tax to the lowest amount possible. A QTIP election was made for the trust, with a reverse QTIP election made for part of the trust equal to the decedent's unused GSTT exemption amount. The will provided that any death taxes incurred by the death of the surviving spouse and directly attributable to the trust were to be paid from the portion of the trust for which the reverse QTIP election was not made. Allocation of trust assets to the two portions was based on the fair market value of the assets on the date of distribution of estate assets to the trust. The IRS ruled that the trust was eligible for a partial reverse QTIP election and that the surviving spouse's right of recovery of taxes resulting from the QTIP portion of the trust did not affect the decedent's status as transferor of the reverse QTIP portion of the trust. **Ltr. Rul. 9337006, June 14, 1993**.

RESULTING TRUST. The decedent was a life beneficiary of a trust established in 1970 by the decedent's sister. The independent trustee improperly transferred the trust corpus, stock, to the decedent's stock brokerage account without the decedent's knowledge. Once the decedent learned about the transfer, the decedent kept the stock separate and only took the net income from the stock. The decedent had made plans to transfer the stock to another trust but died before the transfer was completed. The IRS ruled that the decedent held the stock in a resulting trust under state law and would not be considered as owning the stock; therefore, the stock was not included in the decedent's gross estate. **Ltr. Rul. 9338011, June 22, 1993**.

RETURNS. The IRS has announced that the August 1993 revisions of Form 706 and Form 706-NA are available. The IRS also stated that because of the retroactive application of the OBRA 1993 reinstatement of the 53 percent estate and gift tax rate for cumulative taxable transfers over $2.5 million and 55 percent for transfers over $3 million, the estates which used the February 1993 Form 706 and March 1993 version of Form 706-NA may be liable for additional tax. The IRS will review these returns and assess the additional tax or the estates may lessen the interest by filing amended returns promptly. **Ann. 93-122, I.R.B. 1993-31**.

VALUATION. After the decedent had been diagnosed for cancer with less than a 5 percent chance of recovery, the decedent amended two family partnership agreements to allow the transfer of partnership interests and to have the decedent's son made managing partner at the decedent's death. The decedent transferred remainder interests in the decedent's partnership interests to trusts for the decedent's children in exchange for $250,000 and annuities payable over the decedent's life. The remainder interests were valued using the actuarial tables of Treas. Reg. § 25.2512-5(f) (Table A) for a person of the decedent's age. The annuity agreement had a provision that the remainder interest purchasers agreed to increase the amount to be paid if the remainder interests were revalued by the IRS or Tax Court. The court held that the remainder interests could not be valued using the actuarial table because of the limited life expectancy of the decedent. The savings clause was not effective to change the fact that the purchasers had paid less than fair market value for the remainder interests and that, therefore, the transfers were includible in the decedent's estate as gifts under I.R.C. § 2036 but offset by the $250,000 actually paid. **Est. of McLendon v. Comm'r, T.C. Memo. 1993-459**.

FEDERAL INCOME TAXATION

C CORPORATIONS-*ALM* § 7.02.*

COMPENSATION. The taxpayer, the president of a closely held corporation, claimed that payments from the corporation were repayments of a loan made to the corporation. The court held that the payments were included in the taxpayer's gross income because no corporate records were produced which showed the money paid to the corporation by the president was treated as an obligation of the corporation or that the payments were made on a loan. **Rogers v. Comm'r, T.C. Memo. 1993-444**.

NET OPERATING LOSS. The IRS has adopted as final regulations relating to the segregation of public groups following stock issuances for purposes of determining whether an ownership change has occurred under I.R.C. § 382. The regulations also provide exceptions to the segregation rules in the temporary regulations. **58 Fed. Reg. 51571 (Oct. 4, 1993)**.

COURT AWARDS AND SETTLEMENTS. The taxpayer had filed a suit against a former employer for sex discrimination, sexual harassment, intentional infliction of emotional distress, a common law tort, and breach of contract. The jury awarded the taxpayer $70,000 in compensatory damages and $70,000 in punitive damages on the claim for sex discrimination and sexual harassment, $70,000 in compensatory and $30,000 in punitive damages on the claim for intentional infliction of emotional stress, and $10,000 for the breach of contract. The plaintiff also received costs and attorney's fees. The court held that the $100,000 in punitive damages was included in the taxpayer's gross income because the awards were intended as punishment and not as compensation for injury to the taxpayer. **Reese v. U.S., 28 Fed. Cl. 702 (1993)**.

HOME OFFICE. The taxpayer was a self-employed painter who mostly painted gas stations. The court held that the taxpayer was not allowed deductions for expenses relating to a home office because the taxpayer spent most of the business time painting and the home office could not be considered the principal place of business. **Coutsoubelis v. Comm'r, T.C. Memo. 1993-457**.

The taxpayer was a professor of finance who claimed deductions for expenses related to investment management activities, including a home office. The court held that the investment management activity was not an active trade or business because the lack of current or prospective clients indicated that the activity was not regularly conducted. The court also disallowed the home office deductions because I.R.C. § 280A specifically disallows such deductions for investment activities. **Bendetovitch v. Comm'r, T.C. Memo. 1993-443**.

INVESTMENT INTEREST-*ALM* § 4.03[12].* The taxpayers had investment interest in excess of $10,000 plus investment income and carried the interest disallowed by I.R.C. § 163(d)(1) over to later taxable years until sufficient investment income was available to allow all of the interest as a deduction. The IRS argued that the carried-over interest could not be carried over in subsequent tax years in which the taxpayers' income did not exceed the carried-over interest, because the carried-over interest was not allowable as a deduction in those years *solely* by operation of I.R.C. § 163(d)(1). The Tax Court held that its prior decision in *Beyer v. Comm'r, 92 T.C. 1304 (1989), rev'd, 916 F.2d 153 (4th Cir. 1990)* in favor of the IRS position was incorrect and held that the disallowed investment interest could be carried over without regard to the amount of taxable income in subsequent carryover taxable years. **Lenz v. Comm'r, 101 T.C. No. 17 (1993)**.

INSTALLMENT REPORTING-*ALM* § 6.03.* The taxpayer was a partner in a partnership which sold a building in an installment sale. The partnership reported short term capital gain under the installment method on Form 6252 accompanying Form K-1 for the partners. The court held that the taxpayer could not elect out of the installment method of reporting income from the sale because not all of the gain was reported by the partnership for the return for the year of sale. **Est. of Wilkinson v. Comm'r, T.C. Memo. 1993-463**.

IRA. The taxpayer owned an IRA and was assessed the 100 percent penalty as a responsible person for failure of the taxpayer's company to pay federal employment taxes. The IRS levied against the IRA and the trust company paid the IRA funds to the IRS in partial satisfaction of the penalty. The court held that the taxpayer was liable for the early withdrawal penalty even though the funds were not paid to the taxpayer. **Pilipski v. Comm'r, T.C. Memo. 1993-461**.

PARTNERSHIPS-*ALM* § 7.03.*

ADMINISTRATIVE ADJUSTMENTS. The taxpayer was a tax matters partner (TMP) for a limited partnership. The taxpayer filed a timely individual income tax return for 1984. In 1988, the IRS filed with the taxpayer a Notice of Final Partnership Administrative Adjustment (FPAA) which stated that additional taxes would be due by the taxpayer. The taxpayer signed a Form 870-P agreement to waive the restrictions on assessments resulting from the FPAA and paid the taxpayer's share of additional tax resulting from the FPAA. However, other partners contested the FPAA in the Tax Court resulting in the IRS conceding to drop the additional assessments against the partnership. The taxpayer filed for a refund of the additional taxes paid and brought suit to force the IRS to make the refund. The court held that the waiver agreement was valid and that the refund was barred by the agreement clause in which the taxpayer agreed not to seek a refund unless the taxpayer claimed fraud, malfeasance or misrepresentation by the IRS. Because the taxpayer made no claim of fraud, malfeasance or misrepresentation by the IRS, the refund was denied. **Alexander v. U.S., 93-2 U.S. Tax Cas. (CCH) ¶ 50,536 (N.D. Tex. 1993)**.

PENSION PLANS. The IRS has issued procedures for notifying the IRS that a taxpayer treats businesses as separate lines of business under I.R.C. § 414(r). **Rev. Proc. 94-40, I.R.B. 1993-31**.

The IRS has issued procedures for requesting a determination that a business meets administrative scrutiny as a separate line of business. **Rev. Proc. 94-41, I.R.B. 1993-31**.

The IRS has issued procedures which provide guidelines for simplifying the process of substantiating compliance with the nondiscrimination provisions of I.R.C. §§ 401(a)(4), 410(b):

• Employers who do not have precise data available at reasonable cost may substantiate compliance with the nondiscrimination requirements using reliable substitute data.

Agricultural Law Manual* (ALM). For information about ordering the *Manual*, see the last page of this issue.

• Employers may substantiate compliance with the nondiscrimination requirements using “snapshot” testing on a single representative day.

• Employers may use a simplified method for determining highly compensated employees.

• Employers will not be required to test a plan more than once every three years provided there is no significant change.

• Plan administrators will be able to rely on appropriate, employer-provided information.

• Employers may use many of these substantiation guidelines to demonstrate that they are operating qualified separate lines of business.

Rev. Proc. 94-42, I.R.B. 1993-31.

RENT DEDUCTION. The taxpayer sold several pieces of real property to various foreign entities established by the taxpayers and leased the properties back to themselves. The court held that the taxpayers would not be allowed deductions for rent paid to the entities because the transactions were shams in that the taxpayers retained control over the properties. **Bodor v. Comm’r, T.C. Memo. 1993-456**.

A corporation was allowed deductions for rent paid to a sole shareholder and to a partnership composed of members of the shareholder’s family, where the rent paid was not excessive. **W.H. Braun Family Partnership v. Comm’r, T.C. Memo. 1993-434**.

RETURNS. The IRS has issued a review of the Revenue Reconciliation Act of 1993 changes in tax law for corporations. **Ann. 93-133, I.R.B. 1993-32**.

The IRS has issued guidance for high income individual taxpayers who have additional income tax liability for 1993 resulting from retroactive changes made by the Revenue Reconciliation Act of 1993. The notice also provides guidance on making the election to pay the additional taxes in three installments, including estimating the first installment if the 1993 total is not known. **Notice 93-51, I.R.B. 1993-33**.

S CORPORATIONS-*ALM* § 7.02[3][c].*

ELECTION. The taxpayers filed a timely 1988 S corporation election but failed to provide two items for shareholders’ consent to the election. The election was returned and refiled 15 days late for 1988 and still lacked one consent item. The IRS accepted the election for 1989 and allowed an extension for filing the missing information. The taxpayer argued that the IRS acceptance should apply to the 1988 election and not to 1989 because a clerical error had used 1989 instead of 1988 in the election application. The court held that the election could not apply to 1988 because it was not completely and timely filed in the first place and the clerical error could not be disregarded because the election requirements must be strictly met for a valid election for a certain taxable year. **Garrett & Garrett, P.C. v. Comm’r, T.C. Memo. 1993-453**.

TRUSTS. The taxpayer formed an irrevocable trust funded with S corporation stock. The trust provided for annuity payments to the taxpayer’s sisters and discretionary payments to the taxpayer’s children. Upon the taxpayer’s death, the trust passed to the taxpayer’s children. No distribution could be made in discharge of the taxpayer’s legal obligations to a beneficiary. The taxpayer had the right to substitute property of equal value to the trust property. The IRS ruled that a determination as to whether the taxpayer would be taxed as the owner of the trust property had to be deferred until examination of the income tax returns of the parties involved to determine whether the taxpayer had a nonfiduciary power of administration over the trust. The IRS also ruled that the trust was an eligible Subchapter S trust with the taxpayer considered the owner of the stock. **Ltr. Rul. 9337011, June 17, 1993**.

TRUSTS. The taxpayers, a tax consultant and spouse, transferred their businesses to three business trusts. The court held that the income from the trusts was taxable to the taxpayers as self-employment income because the taxpayers failed to provide any evidence that the organizations were formed for a valid reason except to produce tax deductions and to avoid self-employment tax. **Wilbur v. Comm’r, T.C. Memo. 1993-442**.

NEGLIGENCE

EMPLOYER LIABILITY. The plaintiff was a farm laborer who was injured while hooking a rotovator tiller owned by the defendant to a tractor owned by the plaintiff’s employer. The plaintiff was on the defendant’s land at the time of the accident. The plaintiff did not present any evidence that the defendant employed the plaintiff or authorized the plaintiff to act on the defendant’s behalf. No evidence was presented that the defendant controlled the plaintiff’s labor activities. The court held that the defendant was entitled to summary judgment as to liability as an employer under respondeat superior because the plaintiff failed to show an employment relationship between the parties. In addition, the court held that the defendant’s ownership of the land was not a sufficient basis for imposition of liability. **Gaskins v. Gaona, 433 S.E.2d 408 (Ga. Ct. App. 1993)**.

VETERINARIANS

EXPERT TESTIMONY. The plaintiff was the owner of a black mare which was admitted to the defendant’s care for treatment of an injury to the mare’s hind leg. A black stallion was also admitted to the defendant’s care for removal of chips from the stallion’s front leg. The defendant operated on the wrong horse and the owner of the mare sued for malpractice. After the plaintiff indicated that no expert testimony would be presented, the defendant moved for dismissal, arguing that expert testimony was required by N.H. Rev. Stat. § 507-E:2 to prove medical negligence. The plaintiff argued that operation on the wrong horse was sufficient evidence of negligence and that the statute applied only to cases of injury to humans. The court agreed with the plaintiff but held that expert testimony would be required to prove that the actions of the defendant caused the injury claimed by the plaintiff. Because the case was one of first impression, the plaintiff was allowed to designate an expert witness for trial. **Durocher v. Rochester Equine Clinic, 629 A.2d 827 (N.H. 1993)**.

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WATER

ABANDONMENT. The plaintiff owned a junior ground water right to wells in the Red aquifer and petitioned for abandonment of the water rights of five other wells in the same aquifer. Under Wyo. Stat. § 41-3-104, a petition for abandonment of another's water rights must show a benefit to the petitioner resulting from the abandonment. The plaintiff argued that although it had not demonstrated any specific water use benefit, the abandonment of the wells would produce a benefit in that the relative priority of the plaintiff's water rights in the aquifer would increase. The court held that the benefit claimed by the plaintiff was insufficient to give the plaintiff standing to petition for abandonment of the five wells. Joe **Johnson Co. v. Wyo. State Bd. of Control, 857 P.2d 312 (Wyo. 1993)**.

CITATION UPDATES

Wells Fargo Bank v. U.S., 1 F.3d 830 (9th Cir. 1993), *aff'g*, 91-1 U.S. Tax Cas. (CCH) ¶ 60,067 (C.D. Cal. 1991) (charitable deduction) see p. 145 *supra*.

Commissioner v. Keystone Consolidated Indus., Inc., 113 S.Ct. 2006 (1993), *rev'g*, 951 F.2d 76 (5th Cir. 1992) (pension plans) see p. 99 *supra*. Case remanded to Tax Court, **93-2 U.S. Tax Cas. (CCH) ¶ 50,533 (5th Cir. 1993).**

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